

Joint Legislative Budget Committee

Staff Memorandum

1716 West Adams
Phoenix, Arizona 85007

Telephone: (602) 926-5491
Facsimile: (602) 926-5416

DATE: February 15, 2007

TO: Senator Robert Burns, Chairman, Senate Appropriations Committee
Representative Russell Pearce, Chairman, House Appropriations Committee
Senator Jim Waring, Chairman, Senate Finance Committee
Representative Steve Yarbrough, Chairman, House Ways and Means Committee

THRU: Richard Stavneak, Director

FROM: Steve Schimpp, Assistant Director
Hans Olofsson, Principal Economist

SUBJECT: FY 2008 TRUTH IN TAXATION RATES FOR EQUALIZATION ASSISTANCE
TO SCHOOL DISTRICTS

Summary

By February 15th of each year, the JLBC Staff is statutorily required to report the new Truth in Taxation (TNT) adjustments to K-12 local property tax rates for the upcoming fiscal year. This memo describes the fiscal implications of the estimated TNT adjustments and other related technical estimate updates.

New information from county assessors on property value growth has just been received. Due to higher than expected growth for existing properties, it is now estimated that TNT will require the K-12 Qualifying Tax Rate (QTR) to be lowered 4.5¢ to 9¢ below what was projected in the FY 2008 JLBC Baseline for the Arizona Department of Education (ADE). These new lower rates will go into effect unless two-thirds of the Legislature votes otherwise.

In addition, total statewide net assessed valuation (NAV), which includes both new and existing property and property owned by the Salt River Project (SRP), is 1.9% higher than under the JLBC Baseline. The revised growth rates for both TNT and NAV affect the FY 2008 ADE estimates for Basic State Aid, Homeowner's Rebate, and state property tax collections.

The net impact of these TNT and NAV adjustments would require a \$19.0 million increase relative to the FY 2008 JLBC Baseline for ADE. Property tax revenues from unorganized and minimum QTR districts will also decline by a minimal amount in FY 2008. Table 1 summarizes how this new information could affect the state budget for FY 2008.

Table 1	
Possible Changes to JLBC Baseline	<u>FY 2008</u>
Increase NAV	\$(27,917,400)
Reduce TNT Rates	44,835,400
Increase Homeowner's Rebate	<u>2,042,900</u>
Net Change – Dept. of Education	\$18,960,900

(Continued)

JLBC

There are 4 separate components to the cost estimate. First, the higher-than-projected growth in property values will generate Basic State Aid savings of \$(27,917,400) in FY 2008. Under the K-12 funding formula, a larger tax base generates more school property tax revenues and therefore commensurately less costs to the state. Based on the new valuation data, it is now assumed that statewide NAV (including SRP property) will grow by 15.1% in FY 2008 compared to the JLBC Baseline estimate of 13.2%.

Second, the lower K-12 QTR rates due to the TNT reduction will increase the estimated cost of Basic State Aid by \$44,835,400 in FY 2008 above the current JLBC estimates.

Third, the higher-than-expected NAV growth will also increase the cost for the "Homeowner's Rebate" program (A.R.S. § 15-972). For FY 2008, the state will pay 37% of the cost of residential school property taxes under this program. It is estimated that this cost will be \$2,042,900 higher than is assumed in the current JLBC estimates for FY 2008.

Finally, the revised (lower) QTR rates under TNT will reduce state revenues from certain local property tax collections that are deposited into the state General Fund. However, this impact is expected to be minimal. This will result in a grand total budgetary impact for these technical estimate changes of \$18,960,900 in FY 2008 relative to the current JLBC Baseline.

Background

Pursuant to A.R.S. § 41-1276, the JLBC Staff is required by February 15 each year to compute and report TNT rates for equalization assistance for the upcoming fiscal year. The TNT rates consist of the QTR and the State Equalization Assistance Property Tax Rate, both of which are used in the K-12 funding formula. Note, however, that the state equalization rate is suspended in FY 2007, FY 2008, and FY 2009 as provided by Laws 2006, Chapter 354.

For FY 2007, the QTR is \$3.4788 for unified school districts and \$1.7394 for elementary and high school districts. As noted above, the state equalization tax rate, which applies to all school districts, is \$0. (Prior to Laws 1998, Chapter 153, which extended the TNT legislation to also include K-12 equalization assistance, the corresponding rates were: \$4.40, \$2.20 and \$0.53 per \$100 net assessed value.)

The purpose of TNT is to offset the statewide appreciation of existing property with a commensurate reduction in the QTR and the state equalization tax rate. These rate reductions are intended to ensure that the total statewide tax liability (associated with Basic State Aid) for existing properties remains unchanged in spite of increased valuations.

Revised NAV Growth Rates

Based on new information provided by county assessors, it is currently expected that NAV will grow by 15.2% in tax year 2007 (FY 2008). Of this figure, 8.6% would be attributable to the appreciation of existing property and 6.6% to new construction. After SRP property is included, statewide NAV growth is reduced from 15.2% to 15.1%.

While the final NAV growth rate for FY 2008 will not be known until August of this year, it is expected that only minor adjustments will be made to account for the ongoing assessment of personal property.

New TNT Rates

To comply with the TNT law, the QTR has to be reduced in proportion to the statewide appreciation rate of existing property. Under the original FY 2008 budget estimate, existing property was assumed to grow by 5.6% statewide, which translated into a FY 2008 QTR of \$3.2942 for unified school districts and

(Continued)

\$1.6471 for elementary and high school districts. By comparison, under the revised appreciation rate of 8.6%, the TNT calculation yields a FY 2008 QTR of \$3.2040 for unified school districts and \$1.6020 for non-unified school districts. Pursuant to Laws 2006, Chapter 354, the FY 2008 state equalization rate was left at \$0.

The difference between budgeted and revised TNT rates is summarized in Table 2 below.

Table 2	K-12 Education Tax Rates		
	<u>Unified QTR</u>	<u>Non-Unified QTR</u>	<u>State Equalization</u>
FY 2007 Actual	\$3.4788	\$1.7394	\$0.0000
FY 2008 JLBC Baseline	\$3.2942	\$1.6471	\$0.0000
FY 2008 Revised	\$3.2040	\$1.6020	\$0.0000

Table 2 shows that the original budget lowered the QTR rate for unified school districts by 18.5¢ from \$3.4788 in FY 2007 to \$3.2942 in FY 2008. The newest data results in the QTR being reduced by another 9.0¢ in FY 2008 to \$3.2040.

Total TNT Cost

As shown in Table 3 below, the JLBC Baseline budget assumed a TNT cost of \$90,179,200 for FY 2008. The additional 9¢ QTR reduction that would be required by TNT under revised data would increase this cost by an estimated \$44,835,400. This would result in a total estimated TNT cost of \$135,014,600 for FY 2008.

Table 3	Cost of TNT Reductions	
		<u>FY 2008</u>
Original JLBC Estimate	\$	90,179,200
Possible Revision		<u>44,835,400</u>
Revised TNT Cost		\$135,014,600

A.R.S. § 41-1276 requires that if the Legislature proposes a QTR that exceeds the newly calculated FY 2008 TNT rate, the House Ways and Means Committee and the Senate Finance Committee must hold a joint hearing on or before February 28th and publish a notice of that hearing prior to that date. In addition to publishing a TNT notice, the 2 committees must also jointly issue a press release containing the notice. The Legislature cannot adopt a state budget with rates that exceed the TNT rates unless they are approved in a concurrent resolution by a roll call vote of two-thirds of the members in each house.

RS:SSC:HO:ss

xc: Brad Regens, Director, Fiscal Policy, House
Kitty Decker, Senior Economist, House
Michael Huckins, Appropriations Analyst, House
Mark Bogart, Senior Economist, House
Chris Kotterman, Democratic Research Analyst/Policy Advisor, House
Michael Hunter, Senior Policy Advisor, Senate
Tim Grubbs, Appropriations Analyst, Senate
Sean Laux, Finance Analyst, Senate
Nikki Amberg, Minority Chief of Staff, Senate
Greg Ensell, Minority Policy Advisor, Senate